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E.O. 12958: N/A
TAGS: EFIN ECON EINV PREL KSUM PGOV AR
SUBJECT: Argentina: Finance Secretary on GoA Crisis Response and G-20 Positions

Ref: (A) 08 Buenos Aires 1520
(B) 08 Buenos Aires 1495

Summary

¶1. (SBU) GoA Finance Secretary Hernan Lorenzino told a visiting Senate staffdel February 16 that Argentina's lack of access to international capital markets has insulated it from the impact of the global financial crisis, with Argentina thus far avoiding much of the "social fallout" evident in more developed economies. Lorenzino remains optimistic that the overall impact of the crisis on Argentina will be limited, arguing that Argentina has built up a "cushion" of economic productivity that will allow it to recover quickly from declines in domestic consumption and in international demand for Argentine products. In the near term, the GoA will focus its crisis response on fiscal pump-priming (including via recently announced public works programs and by programs to encourage car and home appliance purchases), on protecting domestic manufacturing competitiveness (especially in the face of newly competitive Brazilian imports), and on preserving domestic employment by "intervening as an arbiter" in union/company labor disputes. He called the GoA's debt burden "manageable," with resources available to cover medium-term maturities without seeking additional international financing. Secretary Lorenzino's upbeat assessment of Argentina's relative insulation from the impact of the global financial crisis stands in contrast to assessments by independent economists, many of whom project zero or negative 2009 GDP growth and the prospect of significant increases in Argentine unemployment and poverty levels in the coming months.

¶2. (SBU) On the upcoming mid-March G-20 Finance Ministers' meeting, Lorenzino called a key Argentine priority working to "re-focus" the IMF on providing minimal-conditionality short-term liquidity lines to allow emerging markets to confront exogenous crises. Argentina has no/no intent to "formalize" any like-minded G-20 sub-group on IMF reforms, he said. "Our goal now is to see emerging markets as a group gain significantly greater representation." Lorenzino called Argentina's position on broad global financial architecture reform generally in line with those of the majority of G-20 members. He highlighted the need for relevant G-20 committees to focus on (1) rating agency reform/oversight; (2) the need to systematically address the "scourge" of tax havens; (3) the need for broad international oversight on the ability of multinational bank headquarters to make "liquidity decisions" on behalf of local bank affiliates that impact emerging market economies; and (4) the need to better regulate the non-transparent credit-default swap market. On multilateral development bank reform, Lorenzino argued that the World Bank has adequate resources to fulfill its development mandate, but that the Inter-American Development Bank needs additional resources. End Summary.

¶3. (SBU) On February 17, Economy Ministry Secretary of Finance Hernan Lorenzino met with Jessica Lewis, Senior Foreign Policy

Advisor to Senate Majority Leader Harry Reid; Caroline Tess, Professional Staff Member, Senate Select Committee on Intelligence; Lieutenant Colonel Richard Root, Office of Congressional Legislative Liaison; and EconCouns to review the GoA's response to the international financial crisis and, in the run-up to the April 2 second G-20 summit in London, to discuss the role the Economy Ministry is playing in G-20 subcommittees on IMF and MDB reform.

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Crisis Impact Ameliorated by Argentine Isolation
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¶4. (SBU) Notwithstanding the severity of the global financial crisis, Lorenzino called its impact to date on Argentina less pronounced than that of other recent crises, including the '94 Tequila crisis, the '98 Russia/Asia financial crisis, the '99 Brazil devaluation, and the market turmoil that followed the 2001 9/11 attacks. "Our isolation (from international capital markets) has helped us," Lorenzino said, insofar as the crisis' initial transmission to emerging markets was largely through financial sector channels. Credit markets have never worked in Argentina, he argued, with less than 30% of the population holding bank accounts and mortgage markets underdeveloped and limited. "This is not a virtue of our financial system by any means," he added, "but merely the reality." As a consequence, Argentina has not experienced the "social fallout" the crisis has had in more developed economies, including via union and anti-immigration demonstrations, Lorenzino argued. The central bank has succeeded in maintaining a gradualist approach to the peso's devaluation and the local financial system is in "good shape," with no Argentine banks at risk of failing, he noted. Although decelerating inflation will impact consumption tax receipts, Lorenzino said, the recent increase in public utility tariffs (via cutbacks in GoA subsidies) will allow the GoA to maintain a fiscal balance.

¶5. (SBU) While fourth quarter 2008 GDP numbers showed a substantial decline and first quarter 2009 GDP performance will be "complicated", Lorenzino said he remains optimistic that the medium-term impact of the crisis will be limited. (Note: According to official GoA statistics, Q4 GDP grew 4.9% y-o-y. In sharp contrast, private analysts estimated that Q4 GDP contracted about 1-1.5% y-o-y.) He argued that the past five years of strong GDP growth have built up a "cushion" of economic productivity that will allow the economy to recover quickly from declines in domestic consumption and in international demand for Argentine products. He called the GoA's debt burden is "manageable," with resources to pay medium-term maturities without access to additional international financing. On Argentina's fiscal balance, Lorenzino said that years of maintaining a positive primary fiscal surplus have given the GoA a base from which to "put pesos into people's pockets" via recently announced public works programs and by programs to encourage car and household appliance purchases.

¶6. (SBU) Beyond fiscal pump-priming to ameliorate the sharp drop in consumer demand, the GoA is also focused on protecting domestic manufacturing competitiveness. February 17-18 bilateral talks in Brazil (in which Economy Minister Carlos Fernandez and Production Minister Debora Giorgi are participating) are focused on limiting any surge in Brazilian imports made very competitive by the substantial crisis-linked depreciation of the Real vs. the Peso. Finally, the GoA will work to preserve domestic employment by "intervening as an arbiter" in union/company labor disputes to ensure that formal sector employment levels are sustained.

¶7. (SBU) In response to Lewis' question on the regional impact of the global financial crisis, Lorenzino called Argentina's biggest concern the health and well-being of Brazil. If the economy of Argentina's single largest trading partner founders, Lorenzino said, Argentina will feel it. "Other countries in the region don't worry me," Lorenzino said, including Chile, which he called better prepared than most in terms of fiscal solvency but highly exposed to the sharp drop in mineral commodity prices. In response to Lorenzino's question on the notable lack of bi-partisan consensus in the recent Congressional vote on the stabilization package, both Lewis and Tess stressed the open dialogue between Democratic and Republican Senators and Congressmen and the quality of debate which helped improve the final stimulus/stabilization package.

Argentina's G-20 Posture

¶8. (SBU) Argentina is well aware of its relative size in the G-20, Lorenzino said, and sees the upcoming mid-March Finance Ministers meeting and April 2 Heads of StateG-20 Summit as "a great opportunity for a small country like Argentina." Lorenzino note that he personally is representing the GoA in the two G-20 sub-committees on IMF and MDB reforms. Argentina has no/no intent to try and "formalize" any G-20 sub-group of like-minded players on IMF reform, Lorenzino emphasized, but is pleased to see that "others are moving towards Argentina's proposals for IMF reform at the first November 2008 G-20 Crisis Summit in Washington. A key Argentine priority at upcoming G-20 meetings will be to work towards consensus on re-focusing the IMF to "creatively" provide minimal-conditionality short term liquidity lines in order to better allow emerging markets to confront exogenous crises.

¶9. (SBU) Lorenzino recalled that Argentina had, in the face of overwhelming member nation support, voted against a 2007 proposal to reform the IMF quota and voting share system. (In this April 2008 IMF vote, 175 member countries favored of the reform and only three member nations - Argentina, Angola, and Palau - voted against it.) "We didn't want this 'set-up' that resulted in Argentina losing both IMF quota and voting share," he explained. "Our goal now is to see emerging markets as a group gain significantly greater representation." On the question of Fund resources, Lorenzino said that Argentina favors giving the Fund more resources, but not without a concomitant change in the way the Fund allocates its money to member nations in need.

¶10. (SBU) The Argentine Central Bank, Lorenzino confirmed, is taking the GoA lead on the other two G-20 working groups ("the working groups most important to the G-7") on enhancing sound regulation and strengthening transparency and on reinforcing international co-operation and promoting integrity in financial markets. He called Argentina's position in these committees in line with those of the majority of G-20 members, albeit with some difference in emphasis. Lorenzino highlighted Argentina's view on the need for these committees to focus more on (1) rating agency reform/oversight; (2) the need to systematically address the "scourge" of tax havens; (3) the need for broad international oversight on the ability of multinational bank headquarters to make "liquidity decisions" that impact local bank affiliate emerging market economies; and (4) the need to better regulate the non-transparent credit default swap (CDS) market. Highly leveraged "speculation" in the CDS market against Argentina, Lorenzino said, had been damaging to Argentina's interests.

11.(SBU) On multilateral development bank reform, Lorenzino argued that the World Bank has adequate resources to fulfill its development mandate but needs to spend its funds more efficiently (Argentina, too, he added, needs to become more efficient in its execution of MDB projects.). In contrast, he said that the Inter-American Development Bank does need additional resources to make additional project funding availale to members.

Comment

¶12. (SBU) Secretary Lorenzino's upbeat assessment of Argentina's relative insulation from the impact of the global financial crisis stands in sharp contrast to assessments by independent economists, many of whom of whom project zero or negative 2009 GDP growth and the prospect of significant increases in Argentine unemployment and poverty levels in the coming months. Lorenzino did, however, acknowledge that sharp drop in fourth quarter GDP that official GoA statistics deny.

¶13. (SBU) On IMF reform, Lorenzino's comments tracked with the 2008 position paper originally submitted by the GoA to the IMF's International Monetary and Financial Committee on behalf of Argentina, Bolivia, Chile, Paraguay, and Peru. This paper called for the Fund to revisit its "excessive" focus on inflationary risks

and its standard recipe for more flexible exchange rates and full capital account liberalization in emerging market economies. Instead, the paper argues that the Fund should focus more on promoting growth in developing countries and support income redistribution policies aimed at boosting consumption. On specific IMF reforms, the paper calls for the IMF to strengthen its policy guidance oversight of developed country economies and to develop an "early warning" system aimed at preventing the recurrence of periodic financial crises. It calls for more emerging market country input into IMF decision-making and the development of a multilateral insurance scheme to better shield developing country members from exogenous shocks. Further, the statement calls for a streamlining of IMF conditionality and a review of access limits and financing terms to bring them into line with developing members' actual potential needs to borrow. The paper concludes that the voice and representation of developing countries within the IMF needs to be expanded beyond the "modest" steps taken in the recently approved quota increase. This includes revisiting the size and composition of the IMF Executive Board, which it characterizes as under-representing developing countries.

¶14. This cable has been cleared by Staffdel Lewis.

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